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Metinvest: "We managed to persuade investors to believe in a company that has experienced a difficult situation over the past few years"

The International Financing Review (IFR) magazine has named Metinvest's debt refinancing as the Emerging EMEA Bond of 2018 in its annual awards, which are among the most prestigious in the global financial community. In an interview with Metal Expert, Alexander Lyubarev, Director of Corporate Finance and Treasury at Metinvest, shared the details and results of the transaction as well as its effect on the investment appeal of the Group and Ukraine as a whole.

Q: Alexander, what goals did Metinvest initially set in terms of refinancing its debt? Was everything achieved through the transaction?

A: The Group did not set the goal of refinancing simply for the sake of refinancing. We were interested in extending the maturity of the debt portfolio; reducing the overall cost of financing; diversifying the base of creditors and investors; and simplifying and, to a certain extent, unifying debt instruments – bonds and syndicated loans. However, our most difficult challenge was to cut the bonds' ties to the pre-export financing facility in order to provide a more stable capital structure and reduce refinancing risks.

Q: Who were the key creditors and investors in the transaction?

A: Our main creditor banks for the syndicated loan are Deutsche Bank, ING, Natixis and UniCredit, with whom we have strong long-term partnerships. At the same time, hundreds of international asset management funds, pension funds and hedge funds with various interests invest in our bonds. For some, it is important to work with a short-term horizon, while others have been cooperating with the Group or investing in its bonds, starting with their first issue in 2010. Hence it was important for us to find a compromise that would suit the interests of all stakeholders.

The refinancing consisted of three simultaneous transactions: a tender for the buyback of the bonds maturing in 2021, along with the modification of their conditions; the issuance of new Eurobonds; and a new version of the pre-export financing facility agreement. If any one of these transactions had not succeeded, nothing would have worked. Most importantly, the transaction is driven completely by market conditions.

Ultimately, Metinvest successfully refinanced debt of US$2.271 billion by issuing two tranches of new Eurobonds totalling US$1.592 billion and devising a new version of the pre-export financing facility agreement equalling US$765 million.

Q: Does this mean there is a high level of trust from creditors?

A: This is a demonstration of the highest level of trust from the investor community worldwide and top European financial institutions. We managed to convince investors to believe in a business that had experienced a difficult situation in Ukraine over the past few years, as well as a period of low steel and ore prices, but also took a responsible approach to its loan obligations.

Regarding the yield at which the bonds were placed and their maturity period, this is certainly a new milestone.

Both issues were placed at the lowest yield in Metinvest's history. In another first, we placed Eurobonds for eight years. There are not very many examples of such a term in Ukraine. Even during the "good" times, in 2010-11, the Group decided not to place bonds for eight years, not only because of the high rate or the difficulty of preparing the issue, but also because it was abnormal for the market. For markets like ours, the usual time frame is five to seven years. Seven years or more is the term at which government bonds are placed. In our case, we managed to place part of the bonds for five years and another part for eight.

At the same time, our goal was not to attract as much capital as possible at any cost for a maximum period. This is not part of the Group's strategy. Of course, any company should manage its liquidity with "long money" as much as possible. In our industry, the cycle ranges from four to seven years, and the longer the resource, the more profitable it is to maintain capital investment.

Q: How difficult was it to find optimal conditions for Metinvest and its creditors? What would have happened if you had not reached a compromise?

A: The Group completed a complex restructuring process in March 2017 and entered the international borrowing market for refinancing only a year later. So the negotiations with creditors were long and difficult.

For this reason, at that time, we did not feel that we had agreed an ideal refinancing rate, primarily on the bonds. At the same time, we secured over US$200 million in new additional funds – by not just issuing new bonds, but also raising new money as part of a syndicated loan. However, as the events of 2018 showed, there was a drastic deterioration in investor sentiment towards emerging markets. If we had entered the market in the autumn, when the Ukrainian sovereign bonds were placed, the rates would have been much higher.

Q: Has the value of Metinvest and its business changed since the refinancing?

A: A stable debt portfolio creates additional value for all stakeholders, both shareholders and debt holders, as well as for the Group itself. Extending the maturity and the early redemption of a substantial part of the repayments for 2018-19 enabled us to reduce Metinvest's debt burden in order to implement the most capital-intensive phase of the capital investment programme.

Q: Does Metinvest still have any unstructured debts? What proportion do they make up and what are their prospects?

A: In March 2017, we completed the restructuring of 94% of the debt portfolio. No restructuring was required for several instruments: the short-term trade financing and the long-term financing of equipment by export agencies. The principled position of shareholders was that these loans be properly serviced even during the most difficult time of the crisis at the end of 2015-16. That is why the restructuring concerned only two main groups of instruments, bonds and syndicated loans.

We have not had any debts that would be in question since March 2017. This is reflected in the credit ratings from international agencies: Fitch, Standard & Poor's and Moody's. Metinvest is one of the few companies in Ukraine that is rated by all three of these agencies. I would say that the Group was able to improve its ratings as a result of the refinancing being limited by the Ukraine's sovereign rating. According to some rating agencies, we have already managed to exceed it.

Q: This was the largest Eurobond issue in the Ukrainian corporate sector. What can it be compared to in terms of scale?

A: If this project is viewed as a joint issue of bonds for one billion and almost six hundred million dollars, then, yes, it is the largest in terms of scale and the most complex, given how it proceeded and what it depended on. I am sure that investors appreciated the fact that even during the most critical moments of 2015-16, we were actively interacting with them and explaining what problems we faced and how we were going to deal with them. Thanks to this, many of them stayed with us even in the most difficult times.

Today, the situation is fairly stable. We understand who we are working with and we know where to go next. Trust and a transparent business are crucial in this regard.

Q: Have there been any transactions in the history of modern Ukraine similar in scale to this?

A: Considering that we are talking about the use of two major instruments, the existence of completely different groups of lenders with different interests, and that this was not a forced bond transaction, we can say that this is unique and one of the best transactions in the history of the Ukrainian private sector.

The situation that Metinvest went through involving the loss of assets in territory not controlled by Ukraine provided us with a unique experience. The prominent European business school INSEAD invited us to talk about how we do business, raise money and carry out a restructuring in a country engulfed in war. These are unique things that are difficult to understand and deserve respect.

Q: What impact has the transaction had on the investment climate in Ukraine as a whole?

A: The success of Metinvest's major debt refinancing, which took into account the interests of all parties, demonstrates the reliability of Ukrainian borrowers to the world financial community. We managed to prove that Ukrainian business is committed to development and is ready to honestly fulfil its obligations despite the unstable political and economic situation.

Q: Do such positive transactions impact the country's rating or not?

A: I believe they have an effect because the preservation of Metinvest's business made it possible to maintain Ukraine's export potential, generate export currency revenue, pay taxes and improve the country's balance of payments. We are less dependent on the devaluation of the hryvnia and pay more taxes, while the state can make repayments when receiving these taxes, including external borrowing on government debt. We support the work of Ukrainian Railways, which, in turn, can service its debts. All told, we provide jobs for people who pay taxes in the same way. Consequently, this is a complex issue and a kind of influence.

Q: Does the Group have any prospects for additional cash flow? What could facilitate this?

A: We are interested in Metinvest's long-term development and we view ourselves as a backbone investor in the economy of Ukraine and countries where we have production assets: Italy, Bulgaria, the United Kingdom and the United States.

In 2017, the Group updated its strategic priorities and Technological Strategy to 2030. First of all, this concerns investments in efficiency: we are not so much increasing production volume as investing in quality, environmental projects, and effectively reducing consumption of various raw commodities, materials and energy resources, among other things.

In 2018, we implemented numerous strategic projects at our metallurgical assets in Mariupol. One key achievement was the construction of the continuous casting machine no. 4 at Illich Steel. Some 30% of the funds for the project were raised under guarantees from the Austrian Export Credit Agency. This is further confirmation that European financial institutions trust Ukraine and Metinvest in particular. Since this is a lower-cost and longer-term credit facility, our strategy is to increase such financing in the Group's debt portfolio.

Q: - What could prevent Metinvest from repaying its debt? What are the main risks?

A: Metinvest intends to fully service its debts since it recognises the importance of long-term relations with creditors.

External factors that could influence the situation include conditions on the raw materials market and the geopolitical situation around and within Ukraine. As far as the raw materials market is concerned, the Group strives constantly to improve its own efficiency. We are working on reducing production costs to ensure competitiveness. This will make it possible to maintain margins during a decline on the market or in prices, i.e. to continue making money on processing or production.

The geopolitical situation in Ukraine is clear. Over the past five years, we have functioned in an unstable environment, and we have learned to work in such circumstances.

As for the business climate in the country, the situation with the most pressing issue for Ukrainian exporters, VAT refunds, has improved significantly over the past few years. This is not to say that the system works flawlessly, but it has become much easier, and we would like this trend to continue.

In Ukraine, Metinvest also faces several issues related to logistics: the rail service, above all from Mariupol to the Black Sea ports, and the passage of ships via the Sea of Azov through the Kerch Strait. We have now managed to resolve issues involving the availability of rail cars and locomotives, as well as the number of trains, that run to and from Mariupol and Kryvyi Rih.

Another problem is that a country like Ukraine does not have an internal market for financing such players as Metinvest. We all understand that the average citizen of Ukraine, with a notional US$1,000, could go to the bank and deposit it at 4% a year. Meanwhile, Metinvest is ready to take on this money at 5% a year for 3-5 years. Such a person must have a mechanism for investing in Metinvest. Unfortunately, the National Bank of Ukraine has a very high key interest rate. Ultimately, Metinvest can obtain financing in hryvnia at a rate of 16% a year at best. We must measure our long-term investment plans with our long-term liabilities for raising money and liquidity. This is an important aspect that must be taken into account.

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